

UNIVERSITY OF SWAZILAND

DEPARTMENT OF ACCOUNTING AND FINANCE

SUPPLEMENTARY EXAMINATION PAPER MAY 2019 ACADEMIC YEAR 2018/2019

PROGRAMME OF STUDY	Bachelor of Commerce
YEAR OF STUDY	Year 3 (Full Time/Part Time)
TITLE OF THE PAPER	Principles of Auditing
COURSE CODE	ACF 316/ AC 316
TIME ALLOWED	Three (3) Hours

INSTRUCTIONS

1. There are **FOUR (4)** questions, **ANSWER ALL**
2. Begin the solution to each question on a new page.
3. The marks awarded for a question are indicated at the end of each question.

NOTE: You are reminded that in assessing your work, account will be taken of accuracy of the language and the general quality of expression, together with layout and presentation of your answer.

THIS PAPER IS NOT TO BE OPENED UNTIL PERMISSION HAS BEEN GRANTED BY THE INVIGILATOR / SUPERVISOR.

QUESTION ONE

Karna (Pty) Ltd was formed 15 years ago by the current managing director, Ben Smith. Karna (Pty) Ltd has 15 members and Ben Smith is the majority shareholder. Karna (Pty) Ltd is in the waste disposal business and has long term contracts with local government bodies to remove and dispose environmental waste. It operates from 30 branches nationwide.

Sam Smith, Ben's son, was appointed as financial director on 30 January 20X10. Sam, who holds a Bachelor of Science degree, is 27 years old and joined the company on 01 January 20X10. Sam has been a friend of yours since school days.

Finalisation of the audit for the year ended February 20X10 has been delayed due to disagreement between the auditor, Jo Gonno, a sole practitioner and management on the accounting treatment of certain structured finance transactions entered into during January 20X10. You are a partner in a medium sized audit firm with offices in all major cities. Sam approached you at the beginning of March 20X10 for your opinion regarding the accounting issues. You agreed with accounting treatment proposed by management. Gonno thereafter agreed to issue an unqualified audit report for the year ended February 20X10. Sam nevertheless asked Gonno to resign as auditor. Gonno refused to issue his audit report and resign, unless he was paid.

Sam offered you the statutory audit appointment subject to your fee quote being acceptable. Sam is of the opinion that the previous fee was too high. During the course of several meetings with senior management to determine the scope of the audit as a basis for your quote, the following information was obtained:

Pat Knox, who was Gonno's audit manager on the 20X10 audit of Karna (Pty) Ltd, was appointed by Karna (Pty) Ltd in July 20X10 to set up an internal audit department which focuses on branch audits.

- Karna (Pty) Ltd was very profitable until two years ago, but profitability has declined since then. For the year ended February 20X11 a small loss was incurred as a result of cuts in local government spending.
- Management responded to the declining profitability by re-engaging the budgetary and target system and introducing an incentive bonus scheme for management based on branch performance
- All branches of Karna (Pty) Ltd use common software packages
- Litigation has been instituted against Karna (Pty) Ltd by an environmental lobby group alleging that the company has been discharging pollutants into certain rivers. The directors are of the opinion that these claims cannot be proven.

- o Each branch controls its own sales and debtors whilst the purchases and creditors functions are centralised

Required

- a) State the matters you would consider in developing your overall audit plan for the year ended 28 February 20X10, assuming you are appointed as auditor of Karna (Pty) Ltd. **20 Marks**
- b) Give the definition for audit risk and each of its components **4 Marks**
- c) Discuss the relationship between the components of audit risk **6 Marks**

(Total Marks 30)

QUESTION TWO

- a) The following are 10 audit procedures taken from an audit program
 1. Confirm accounts payable balances directly with vendors
 2. Account for a sequence of checks in the cash disbursements journal to determine whether any have been omitted
 3. Examine vendors' invoices to verify the ending balance in accounts payable
 4. Compare the balance in payroll tax expense with the previous years. The comparison takes the increase in payroll tax rates into account.
 5. Examine the internal auditors' initials on monthly bank reconciliations as an indication of whether they have been reviewed
 6. Examine vendors' invoices and other documentation in support of recorded transactions in the acquisitions journal
 7. Multiply the commission rate by total sales and compare the result with commission expense
 8. Examine vendors' invoices and other supporting documentation to determine whether large amounts in the repair and maintenance account should be capitalized
 9. Discuss the duties of the cash disbursement clerk with him and observe whether he has responsibility for handling cash or preparing the bank reconciliation
 10. Inquire about the accounts payable supervisors' of a computer generated exception report of receiving reports and purchase orders that have not been matched with a vendor invoice

Required

- i. Indicate whether each procedure is a test of control, substantive test of transactions, analytical procedure or a test of details of balances **(10 Marks)**
 - ii. Identify the type of evidence for each procedure e.g. analytical procedure, confirmation etc. **(10 Marks)**
- b) Management typically has three broad objectives in designing effective internal controls. Identify and briefly describe these. **(5 Marks)**

(Total Marks 25)

QUESTION THREE

- A. Match the parts of statements in list A to those in list B to complete a correct full statement **(20 Marks)**

List A

- A1 *The objective of the auditor is to plan the audit....*
- A2 *The overall audit strategy sets the.....*
- A3 *Special audit consideration should be given to*
- A4 *The fact that an audit client is listed on the JSE will influence....*
- A5 *The audit plan lays out, inter alia, the.....*
- A6 *The compilation and signing of the engagement letter is the final step in.....*
- A7 *The extent of testing will depend largely on assessed risk and.....*
- A8 *Involving the key members of the engagement team in the planning process enhance the...*
- A9 *The appropriateness of audit evidence relates to its.....*
- A10 *Increasing the supervision of the audit team will be an overall response to address....*

List B

- B1 *...significant risks*
- B2 *...relevance and reliability*
- B3 *...effectiveness and efficiency of the planning process*
- B4 *...so that it will be performed in an efficient manner*
- B5 *...materiality limits*

- B6 ...the overall audit strategy
B7 ...nature, timing and extent of planned risk assessment procedures
B8 ...assessed risk at the financial statement level
B9 ...the preliminary engagement activities
B10 ...scope, timing and direction of the audit

(Total Marks 20)

QUESTION FOUR

You are the senior partner of NoChange Inc., a medium audit firm based in Paarl. You are also the auditor of Purl Valli Golf Estates and Spa. The fieldwork for the audit for the year ended 30 September 20X9 has been completed and no material misstatements have been identified. All audit differences that existed at year end have been satisfactorily resolved.

The only outstanding matters regards to the audit, before the audit report can be issued, are the procedures relating to subsequent events and going concern. Once these procedures have been performed, the audit report can be issued, as management has almost completed the financial statements as well.

Required

- a) Prepare the audit report to the members of Purl Valli Golf Estates and Spa assuming that it is appropriate to prepare the financial statements on a going concern basis. **25 marks**
- b) Explain the effect on the auditor's report if the auditor is of the opinion that a material uncertainty regarding an organization's going concern position exists **5 Marks**

(Total Marks 25)

.....**END OF PAPER**.....